United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

75-5019

United States Court of Appeals

FOR THE SECOND CIRCUIT

B.

P/S

In the Matter of

CARTRIDGE TELEVISION, INC.,

Bankrupt.

EDDIE L. THOMPSON, JR., EDWARD A. NEFF, SUE MANCINI, DAVID D. ACKERMAN, BILL COPSES, BILL DIANGIKES, JOHN F. MAGDA, J. HIRAM JOHNSON, DEAN ELLISON, and ROBERT KELLER, as Pension Fund Trustee,

Appellants,

—against—

STANLEY TULCHIN, as Trustee-in-Bankruptcy of Cartridge Television, Inc.,

Appellee.

APPELLEE'S BRIEF

OTTERBOURG, STEINDLER HOUSTON & ROSEN, P.C.
Attorneys for Appellee
230 Park Avenue
New York, New York 10017
(212) 679-1200

Of Counsel:
CONRAD B. DUBERSTEIN, Esq.
M. DAVID GRAUBARD, Esq.

2

TABLE OF CONTENTS

TABLE OF CASES

TABLE OF STATUTES

Table of Authorities

United States Court of Appeals

For the Second Circuit

Docket No. 75-5019

In the Matter of

CARTRIDGE TELEVISION, INC.,

Bankrupt.

EDDIE L. THOMPSON, JR., EDWARD A. NEFF, SUE MANCINI, DAVID D. ACKERMAN, BILL COPSES, BILL DIANGIKES, JOHN F. MAGDA, J. HIRAM JOHNSON, DEAN ELLISON, and ROBERT KELLER, as Pension Fund Trustee,

Appellants,

—against—

STANLEY TULCHIN, as Trustee-in-Bankruptcy of Cartridge Television, Inc.,

Appellee.

APPELLEE'S BRIEF

Statement of Issues Presented for Review

1. Whether the determination by the Bankruptcy Judge that under the attendant circumstances of this case, the claims filed by the Appellants (hereinafter "Claimants") should be disallowed pursuant to Section 57d of the Bankruptcy Act is violative of the Due Process Clause of the Fifth Amendment to the United States Constitution.

2. Whether the claims filed by the Claimants in this Bankruptcy proceeding were properly filed as "Class Claims."

Statement of the Case

This appeal arises out of a bankruptcy proceeding that followed an aborted Chapter XI arrangement proceeding before the Honorable Asa S. Herzog, Bankruptcy Judge. The Claimants filed Claims No. 533 and 534 (hereinafter "Claims") as class representatives alleging fraud and various violations of the Securities Act of 1933 and 1934.

The Appellee (hereinafter "Trustee") objected to these Claims by a notice of motion and petition (9a)*. After a hearing and submission of legal memoranda, Judge Herzog rendered a decision on June 3, 1975, sustaining the Trustee's objections to the Claims (15a). On June 9, 1975, an order was made by Judge Herzog disallowing and expunging the Claims from this bankruptcy proceeding(23a). A fully conformed copy of Judge Herzog's order was not included in the Joint Appendix, but is annexed to this brief as Exhibit "A."

An appeal was taken by the Claimants (25a). After oral argument and submission of legal memoranda, an order was made by the Honorable Kevin T. Duffy, United States District Judge, affirming the order of Judge Herzog. A copy of Judge Duffy's order was not included in the Joint Appendix but is annexed to this brief as Exhibit "B." A copy of the relevant docket entries taken from the Office of the Clerk in the Court below was not included in the Joint Appendix but is annexed hereto as Exhibit "C."

The Claimants have appealed from Judge Duffy's order which brings the matter before this Court.

---

* Page references are to the Joint Appendix.

Facts

The attorneys for the Trustee and the attorneys for the Claimants entered into a Stipulation of Facts dated March 24, 1975 (13a). The Court is respectfully referred to this Stipulation for the relevant facts herein.

Summary of Lower Courts' Decision

Judge Duffy affirmed Judge Herzog's order with a memo endorsed, and in effect, adopted the reasoning set forth by Judge Herzog in the latter's decision and order.

The Bankruptcy Court initially determined that there was no authority for the class status asserted by the Claimants in their Claims. Therefore, Judge Herzog disallowed these Claims insofar as they represented claims on behalf of the purported "class members" and treated them as claims filed by the two persons named in No. 533 and the nine persons named in No. 534.

The Bankruptcy Judge then considered the status of these Claims in light of Section 57d of the Bankruptcy Act. He determined that both Claims were indeed not capable of liquidation or of reasonable estimation, and that such liquidation or estimation would unduly delay the administration of the bankrupt estate (20a).

The Bankruptcy Judge noted that the intent of Congress was to see that the Court's discretion in applying Section 57d was "used in a generous and liberal way, *with due regard, however, to the rights of other creditors.*" (21a)

Clearly, Judge Herzog weighed *all* of the factors in this case. He examined the Claims of the Claimants, considered

the rights of the other creditors of this estate, and viewed the status of the lawsuits commenced by the Claimants in the District Court; and after deliberating upon all of these elements, made the determination that Section 57d should be applied to the Claims herein. The Trustee maintains that the Bankruptcy Judge was correct in his determination and did not abuse his discretion in applying Section 57d to these Claims.

POINT I

Section 57d of the Bankruptcy Act is in the nature of a statute of limitations.

The duty of the Bankruptcy Court to examine unliquidated or contingent claims is undisputed. Bankruptcy Act, Section 2a(2); 11 U.S.C. § 11a(2).

> "The proviso of ¶ 57(d)[sic] of the Act indicates that it is incumbent upon the court, when an unliquidated or contingent claim comes up for allowance, to determine whether it is potentially capable of liquidation or estimation, and if so, whether its liquidation or estimation will unduly delay the administration or proceedings." 2 *Remington on Bankruptcy,* § 855, p. 31.

The present Section 57d of the Bankruptcy Act has a proviso that was part of the Chandler Act of 1938 which reads as follows:

> "*Provided, however,* that an unliquidated or contingent claim shall not be allowed unless liquidated or the amount thereof estimated in the manner and within the time directed by the court; and such claim shall not be allowed if the court shall determine that

> it is not capable of liquidation or of reasonable estimation where such liquidation or estimation would unduly delay the administration of the estate or any proceeding under this Act."

As can be seen from a reading of this proviso, it sets certain guidelines for limiting contingent and unliquidated claims. By doing so, it attains the nature of a statute of limitations.

A section of the Bankruptcy Act which is highly analogous in this statute of limitations principle is Section 57n which has established a time limit for the filing of claims in a bankruptcy proceeding. Claims *must* be filed within six months after the date of the first meeting of creditors or they will not be allowed. This has been reiterated by Rule 302(e) of the Rules of Bankruptcy Procedure.

Other than certain statutory exceptions provided for in Section 57n, a creditor in a bankruptcy proceeding who fails to file his claim within the six month period is barred from participating in the distribution from the bankrupt's estate regardless of the *bona fides* of his claim. No late claim will be allowed to share in the distribution proceeds unless all claimants who properly filed are paid 100 percent of their claims.

The definitive time limit established by Section 57n constitutes a mandatory legislative expression. See: 3 *Collier on Bankruptcy,* 14th ed., ¶ 57.27, p. 415. This idea has been expressed in various cases cited therein, but it is punctuated in the case of *In re Brill,* 52 F.2d 636 (SDNY, 1931), *aff'd,* 52 F.2d 639 (2nd Cir., 1931), in which the Court characterized Section 57n as follows:

> "This is a statute of limitations. It is even more. It is a prohibition. It is peremptory." (52 F.2d at 637).

Just as Section 57n establishes a time limit within which all claims must be filed in a bankruptcy proceeding, so too Section 57d sets a time limit for the liquidation of contingent claims, which is necessary for the orderly administration of a bankrupt estate. Whereas Section 57n is strict in its application, Section 57d is flexible and the application thereof will depend upon the facts of the individual given situation.

The concept underlying a statute of limitations is a firmly established principle in American Law. Section 11 of the Bankruptcy Act, 11 U.S.C. § 29, sets forth specific statutes of limitations regarding actions involving bankrupts and bankruptcy proceedings. As noted above, Section 57n sets forth another statute of limitations. Accordingly, Section 57d must be viewed in its proper perspective, i.e., as a statute of limitations within which a contingent or unliquidated creditor must prove and liquidate his claim. Whereas the other sections cited above deal with express statutory time limits, Section 57d, by its very terms, provides for a less rigid statute of limitations which must be determined by the Bankruptcy Court on the facts underlying each individual case.

Generally, *no matter how meritorious a person's claim,* if he does not comply with the applicable statute of limitations, his claim will be barred. This rule applies whether in respect to initiation of a lawsuit or arbitration, or to filing a claim in a bankruptcy proceeding. In the case at bar, it has been determined that the Claimants have not complied with the relevant statute of limitations (i.e., Section 57d) and, accordingly, the Claims have been properly disallowed from this bankruptcy proceeding.

POINT II

The application of Section 57d must be considered in light of the posture of the bankruptcy proceeding and the Claimants' lawsuits.

We have already noted that Section 2a(2) of the Bankruptcy Act imparts to the Bankruptcy Court the obligation to examine unliquidated and contingent claims (*supra*, p. 4). Section 57d lays the groundwork for the procedure to be followed when an unliquidated or contingent claim has been filed which inhibits the closing of the bankrupt estate.

Section 63d is a complement of Section 57d and provides for the nonprovability of claims that are disallowed under Section 57d. The concept which underlies both these sections is considered to be one of the paramount objectives of the bankruptcy proceedings, i.e., expeditious administrative of bankrupt estates. 3 *Collier, supra,* ¶ 57.15, p. 247. Therefore, the rights of a claimant against whose claim there is an objection based on Section 57d *must* be weighed against the rights of all the other creditors in the bankruptcy proceeding.

The Claimants have taken the position that any Bankruptcy Judge who disallows a claim pursuant to Section 57d in a corporate bankruptcy has *ipso facto* abused his discretion. The Trustee maintains that to "brush with such a broad stroke" is improper and that each case must be evaluated on its own individual facts.

In Point I of their brief, the Claimants allege that "[t]he application by the Bankruptcy Judge of his discretion under Section 57(d) [sic] of the Bankruptcy Act *in the instant case* is an abuse of discretion." (Appellants' brief,

p. 3, emphasis in original). To the contrary, the Trustee asserts that when *all the facts* surrounding these Claims and this bankruptcy proceeding are considered, it is clear that Judge Herzog's determination was manifestly correct and that his decision (15a) and order (23a) did not constitute an abuse of discretion.

The posture of the present bankruptcy proceeding is germane to this appeal. When the Chapter XI proceeding was converted to a straight bankruptcy proceeding, all of the bankrupt's assets were encumbered by a lien in favor of Avco Corporation ("Avco"). By an order of Judge Herzog, dated January 27, 1975, the Trustee was authorized to settle the Avco lien claim which liquidated *all* the assets in this estate. This order was appealed by the Claimants herein and affirmed by an order of the Honorable Inzer B. Wyatt, United States District Judge, on May 6, 1975. No further appeal was taken.

The Trustee has examined all the claims filed in the bankruptcy proceeding and has already made approximately forty objections thereto. Only five objections are still pending, all of which have been adjourned to February 18, 1976. It is expected that these five objections will be resolved by the adjourned date. When these objections are completed, since all the assets of the bankrupt have been liquidated, this estate will be ready to be closed and distribution made to the creditors. The Trustee has on hand approximately $800,000.00 which will be disbursed amongst creditors whose claims aggregate roughly $3,000,000.00.

The Claimants herein are shareholders of the bankrupt. Normally, shareholders have no right to participate as creditors in a bankruptcy proceeding.

> "Courts have repeatedly frowned upon the attempt of a stockholder at the bankruptcy to 'lay aside the garb of a stockholder, on one pretense or another, and to assume the role of a creditor.'" *In re Groenleer-Vance Furniture Co.*, 23 F. Supp. 713 (W.D. Mich., 1938) p. 715.

The question of shareholders *vis-a-vis* general creditors involves the issue of equity versus debt. Shareholders by their very nature are conscious risk-takers. They are not creditors of a corporation. They do not enjoy a creditor-debtor relationship with the corporation. Shareholders are the holders of corporate equity whose rights are subordinated to those of general creditors. The Claimants herein, by alleging fraud, now try to elevate themselves to the status of general creditors. To date, they have nothing that attributes to this status other than two lawsuits commenced by them in the United States District Court, Southern District of New York.

These lawsuits are two class actions by the Claimants based on their transactions with the bankrupt, bearing Index Nos. 74 Civ. 732 (MEF) and 74 Civ. 1802 (MEF). The bankrupt was named as a defendant in the first action which has allegations similar to those asserted in the Claims. The second action is against a stock brokerage firm and several of its officers and employees, and alleges fraud and securities violations independent of the Claims.

Those lawsuits originally alleged class action status. The first one names over twenty defendants as well as various "John Does" and "Richard Roes." The named defendants in the first action include Avco (a substantial investor and stockholder of the bankrupt), an accounting firm, a stock brokerage firm, and various officers of Avco and the bank-

rupt. By an order of the Honorable Marvin E. Frankel, United States District Judge, dated July 2, 1975, the class status allegations in both these lawsuits was stricken. At that time, these suits were then continued in the name of the various plaintiffs named therein. However, at this time, only Eddie L. Thompson, Jr. remains as a plaintiff, the other plaintiffs having withdrawn from both lawsuits. The lawsuits were commenced on February 14, 1974, and April 24, 1974, respectively. Both cases have demanded trial by jury.

In the first action, the accounting firm of Arthur Young & Co., one of the defendants, moved for summary judgment. This was granted by the District Court and the plaintiff appealed. This Court of Appeals affirmed the District Court's grant of summary judgment by an order dated July 26, 1975.

All of the defendants who have been served in the lawsuits are vigorously defending both actions. Preliminary interrogatories have been served and it is reasonably expected that pre-trial discovery may very well continue for many, many months, if not for several years.

A reading of the complaints filed in both actions, as well as a survey of the activity that has been generated in these cases as evidenced by the entries on the District Court's docket, clearly indicates that these cases involve complex issues of fact and of law which will entail lengthy trials. Moreover, there are indications that whatever the outcome, the unsuccessful party or parties would undoubtedly appeal, further elongating the lives of these lawsuits. It certainly is not unreasonable to expect that a minimum of five to six years will be required for the ultimate determination of these lawsuits. With due regard to the amount of discovery that is expected in *both* of these lawsuits and the

expected time for trial, it seems reasonable that the five to six year figure may only be a *minimum* estimate.

The Claimants have not disputed that their Claims fall within the proviso of Section 57d. The Bankruptcy Judge, after having determined that the Claims were not class claims but would be considered as claims on behalf of the persons named therein, went on to determine that those claims as modified were still within the proviso of Section 57d. The Claimants do not question the propriety of that finding, but only the validity of that Section as it is applied to this proceeding.

It must be emphasized that the Claims are wholly contingent. The lawsuits commenced by the Claimants sound primarily in tort and are consistent with the assertion made by the Claimants herein at Page 2 of their Brief that they are "defrauded stockholders."

It is vitally important to note that the Trustee strenuously objects to the merits asserted by the Claimants in both their bankruptcy claims and the lawsuits. This is not a question of reconciling a claim which the Bankruptcy Court or the Trustee believes has merit (as was done in *In re Four Seasons Nursing Centers of America, Inc.*, 472 F.2d 747 (10th Cir., 1973) [a Chapter X proceeding]). The Trustee firmly believes that the Claimants' Claims are without foundation and are not entitled to participate in this bankruptcy proceeding on a par with the general creditors of the bankrupt.

Therefore, consideration of the Claimants' arguments must involve the weighing of the rights of *bona fide* creditors whose claims aggregate about $3,000,000.00 against those of the Claimants (1) who are stockholders of the bankrupt; (2) who have alleged fraud; (3) whose claims

are contingent; and (4) who are *not* general creditors of the bankrupt. The stockholder-Claimants would have the bankruptcy proceeding held in abeyance for at least another five to six years thereby depriving the existing, duly proven creditors of this bankrupt estate of the orderly and expeditious administration thereof which would result in the distribution they are entitled to in accordance with the Bankruptcy Act.

If the Claimants' argument is correct, then in every case involving a corporate bankruptcy, the shareholders could allege a fraud and thereby delay the administration of the bankrupt estate for many years. This would work an undue hardship on the recognized creditors of the bankrupt, delay the administration of bankrupt estates, create a huge backlog in the Bankruptcy Courts around the country and thoroughly undermine the purpose and procedures of the Bankruptcy Act. Moreover, this would virtually encourage stockholders to assert fraud claims, *no matter how frivolous,* with the hope of harassing the bankruptcy trustee into a settlement in order to avoid delaying the administration and distribution of the estate, all to the detriment and prejudice of general creditors.

It is therefore clear that the application of Section 57d to the Claims herein must be weighed and considered in conjunction with the status of the within bankruptcy proceeding and the Claimants' lawsuits.

POINT III

Section 57d may be validly applied to a corporate bankruptcy proceeding.

The Claimants aver that Section 57d as applied to the instant case violates the Due Process Clause of the Fifth Amendment to the United States Constitution. The Trustee

maintains that a balance *must* exist between the expeditious administration of bankrupt estates and the allowance of unliquidated and wholly contingent claims which are disputed and may eventually be determined not to be *bona fide* claims at all.

This "balance argument" is a valid judicial procedure in due process cases, *United States* v. *Weiler*, 458 F.2d 474 (3rd Cir., 1972), p. 480. The Trustee urges that considering all the factors in this bankruptcy proceeding and the facts surrounding the Claims at issue herein, the scales favor the disallowance of these two Claims, and Section 57d of the Bankruptcy Act is not violative of the Fifth Amendment's Due Process Clause.

The applicability of Section 57d to a corporate bankruptcy was considered in the case of *In re Hot Springs Broadcasting, Inc.*, 210 F. Supp. 533 (W.D. Ark., 1962), in which the appellant therein had filed a claim for "radio programming service" without attaching a contract, statement or invoice to the proof of claim. The Bankruptcy Court found two defects in the claim: (1) it did not conform to Section 57b concerning the form of a proof of claim; and (2) it was "not capable of liquidation or of reasonable estimation" (p. 537) and therefore was disallowed under Section 57d of the Bankruptcy Act.

On review to the District Court, the Bankruptcy Court's determination under Section 57d was sustained. Although the reviewing Court disagreed with the Bankruptcy Court's determination under Section 57b, the Court affirmed the disallowance of the claim under Section 57d.

> "Although this court has found that the Referee erred in concluding that there was no valid contract between the claimant and the bankrupt on the date

> of bankruptcy, yet the court is of the opinion that the order of the Referee disallowing the claim of claimant should be approved and confirmed for the reason that the proof of claim did not conform to [11 U.S.C.] Sec. 93 sub. b; that the claim was unliquidated and was not liquidated or the amount thereof estimated in the manner and within the time directed by the court; and that *such liquidation at the time the order was entered disallowing the claim on October 1, 1962, 'would unduly delay the administration of the estate.'* [*11 U.S.C.*] *Sec. 93, sub. d of the Bankruptcy Act.*" (210 F. Supp. at 544)

The issue of creditors with unliquidated and contingent claims against a corporate bankrupt has previously been considered by the United States Supreme Court. In *Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U.S. 320, 54 S.Ct. 385, 78 L.Ed. 824 (1934), the Court had before it a claim of a landlord who sought to prove in bankruptcy the loss of rents for the remainder of the lease term, based on various provisions of the lease. This case arose before the 1938 expansion of Section 63a of the Bankruptcy Act which added to the category of provable debts.

The claims of appellants therein were expunged because the Bankruptcy Referee found that the loss of future rents did not constitute a provable debt. This determination was affirmed by the District Court and the Court of Appeals for the Second Circuit.

The appellants therein argued that the expunging of their claim worked an

> "unfairness to the landlord of a corporate bankrupt who, under the decision below, cannot prove upon his lease along with other creditors, but must look solely

> for redress for loss of future rents to a corporate debtor whom bankruptcy has stripped of all assets." (291 U.S. at 331-332).

The Supreme Court considered the arguments of the appellants and the provisions of the leases upon which they sought to prove their claims and affirmed the expunging of the claims, concluding that "[t]he covenants appearing in the leases in question cannot be made the basis of a proof of debt against the estate." (291 U.S. at 339).

The *Manhattan Properties* case, *supra,* was followed in *Shultz* v. *Irving Trust Co.,* 74 F.2d 121 (2nd Cir., 1934), in which a corporate bankrupt had incurred an obligation to pay for structural changes made by the landlord which were amortized over the life of the lease. When the petition in bankruptcy was filed, there remained 46 years on the 50-year lease. The Court found that these charges were not provable as they were contingent on the occupation of the premises by the bankrupt. The claim was disallowed even though the bankrupt was a corporation.

The *Manhattan Properties* case was followed in *In re F. & W. Grand 5-10-25 Cent Stores, Inc.,* 74 F.2d 654 (2d Cir., 1935) and *Kennedy* v. *Boston-Continental National Bank,* 11 F. Supp. 611 (D.C. Mass., 1935).

Section 57d of the Bankruptcy Act has been given wide application since its inception. In *Nathanson* v. *National Labor Relations Board,* 194 F.2d 248 (1st Cir., 1952), the Bankruptcy Court disallowed the claim filed by the NLRB. The District Court reversed and the Trustee appealed. On the question of undue delay, the Court of Appeals cited the NLRB's own brief for the principle that Section 57d of the Bankruptcy Act applies where the liquidation of a claim would unduly delay the administration of the estate. The

Nathanson case concerned a corporate bankrupt and the Court acknowledged that had the NLRB been remiss in commencing its administrative proceedings, then disallowance under 57d would be appropriate. (194 F.2d at 251).

The Trustee initially maintains that the two Claims filed herein sound in tort, as they are based on fraud. Stipulated Facts No. 2, 4 and 5 (13a-14a) indicate that these are basically fraud claims. Of course, if these claims are pure tort claims, they are not provable under Section 63 of the Bankruptcy Act and should properly be disallowed from this proceeding. 2 *Remington, supra,* § 815, p. 229.

However, without making any findings, the Bankruptcy Judge assumed *arguendo* that Claims No. 533 and 534 might be initially provable on the basis of breach of an implied contract. Following the Bankruptcy Judge's *arguendo* reasoning, Congress through the exercise of its bankruptcy powers, can constitutionally pass legislation, that amongst other things, ". . . may impair or destroy the obligation of private contract . . ." *Ginsberg* v. *Lindel,* 107 F.2d 721 (8th Cir., 1939), p. 726.

Although *Ginsberg* v. *Lindel, supra,* concerned vested property rights of the claimant, it acknowledged that "[t]here is, however, a significant difference between a property interest and a contract . . ." (107 F.2d at 726).

In the instant case, even assuming that an implied contract existed between the Claimants and the bankrupt, Congress, through Section 57d of the Bankruptcy Act, may affect the obligation of that contract. This is especially so where the claim is contingent and unliquidated, and where the liability on behalf of the bankrupt is ethereal in nature and may never become an actual, fixed liability.

The Claimants cite *In re William Rakestraw Co.*, 450 F.2d 6 (9th Cir., 1971), which is factually different from the case at bar and has no application hereto. A reading thereof shows that Mr. Rakestraw contracted with the claimant for the purchase of a store. Thereafter, he formed a corporation (the bankrupt therein) and the issue in that case concerned the understanding that the bankrupt company was to assume certain personal obligations of Mr. Rakestraw.

The claimant therein had obtained a judgment against Rakestraw personally and the only issue was the liability of the bankrupt as the assignee of Mr. Rakestraw. As distinguished from the case at bar, in *Rakestraw* the claimant had a liquidated claim, and the only question was the liability of the bankrupt corporation for the personal obligation of Mr. Rakestraw.

The Claimants herein have claims that are wholly unliquidated and contingent. In *Rakestraw,* there was a liquidated amount (evidenced by the judgment obtained against Rakestraw personally) with the sole question being that of corporate liability. Accordingly, the *Rakestraw* case is inapposite and not applicable to our situation.

The Claimants maintain that the Fifth Amendment restrictions apply to bankruptcy proceedings. In view of the supremacy of the United States Constitution, the Trustee does not take issue with the applicability of the Constitution to bankruptcy proceedings. However, the Trustee does maintain that the application of Section 57d to the claims considered herein is not unwarranted in view of the nature of those claims and the District Court lawsuits upon which they are based.

"Due process of law means, essentially, fundamental fairness." *United States* v. *Mason,* 232 F. Supp. 102 (S.D.

N.Y., 1964), p. 110. "The due process clause of the Fifth Amendment is essentially a recognition of the principles of justice and fundamental fairness in a *given set of circumstances, . . .*" *Honneywell, Inc.* v. *Metz Apparatewerke,* 509 F.2d 1137 (7th Cir., 1975), p. 1143 (emphasis added). The essential test then, is whether the application of Section 57d to the Claims herein, *taken in the context of all the attendant circumstances,* provides the basic fairness to the Claimants *and* to the other creditors of the bankrupt in consonance with the Fifth Amendment.

The purpose of Section 57d is "to guard against undue delay incident to the admission to proof of any contingent or unliquidated claim." 3 *Collier, supra,* ¶ 57.15[3], p. 254. This is consistent with the purpose of the proviso of Section 57d that was enacted by Congress in 1938.

The hearings before the House of Representatives explain the reasons for the proviso. The idea was to allow contingent claims that could be fully liquidated and proved *after* the bankruptcy proceeding had been commenced but *before* the bankrupt estate was closed and the assets distributed amongst the claimants in the bankruptcy proceeding. This is evident from the House Hearings:

> "Mr. Hunt: Section 57 is on page 175. All of my references are to the committee print. It is on line 7. That refers to proof and allowance of claims.
>
> There are changes of phraseology there. Then there is also a provision that contingent claims can be proved and allowed provided they can be liquidated before the final disposition of the case and before the assets are all distributed.
>
> Not in all countries, but in the English and the Canadian bankruptcy acts, they have a provision for

> the proof and allowance of contingent claims, but we have not had that in our act, even though the *claim could be liquidated before the close of the proceedings without harm or prejudice to anyone.* This brings that idea into our act. We think it is rather a salutary provision.
>
> Mr. Michener. This puts a contingent claim on the same footing as another claim?
>
> Mr. Hunt. Providing it can be liquidated *before the estate is closed, without prejudice to the other creditors.* Provided there is cash on hand." House Hearings on H.R. 8046, 75th Cong., 1st Sess. (1937), pp. 114-115 (emphasis added).

The intent of the proviso was to prevent the unwarranted prolongation of the administration of bankruptcy estates. The interests of *bona fide* creditors had to be and was balanced against the claims of contingent creditors. Further on in the House Hearings, this precise issue arose:

> "Mr. Michener. It will not permit the holding up of the case by the filing of contingent claim?
>
> Mr. Hunt. *That might not be liquidated for years?* No; that cannot be done. That does not follow." House Hearings on H.R. 8046, *supra,* p. 115 (emphasis added).

The same understanding existed in the Senate. The proviso of Section 57d was patterned after the English Bankruptcy Act which had a broad scope for allowing contingent claims. However, the proviso was not open-ended with regard to all contingent and unliquidated claims, and conditioned the allowability of such claims on the liquidation and proving thereof within a reasonable period of time, without prejudicing the other creditors of the bankrupt.

> "The House bill attempts to extend the allowability of such claims to classes where the contingency occurs *before* the declaration of a final dividend or before the confirmation of a settlement under the debtor relief chapters." Senate Report No. 1916, 75th Cong., 3d Sess. (1938), p. 5 (emphasis added).

A review of the foregoing cases and portions of the Congressional hearings shows that the application of Section 57d must be made after considering the rights of *all* creditors of a bankrupt, and that after due consideration Section 57d may be validly applied in a corporate bankruptcy proceeding.

POINT IV

Section 57d was properly applied to the Claimants' claims in this bankruptcy proceeding.

The underlying principle of expeditious administration of bankruptcy estates, which pervades Section 57d as well as the entire Bankruptcy Act, has been followed by legal commentators.

> "Contingent claims, that is, those uncertain as to whether there *will ever be any liability,* are not precluded from proof and allowance as the statute now stands, and were considered provable and allowable even prior to the specific statutory provisions to that effect unless they were 'too contingent.' Section 57(d) [sic] of the Act, however puts them in the same category with unliquidated claims by retracting their provability unless actually allowed." 2 *Remmington, supra,* § 865, p. 323 (emphasis added).

As is evident from the hearings before the House and the Senate, and from the very words of the proviso of Section 57d itself, the procedure of proving and liquidating a contingent claim must be accomplished before the bankrupt's estate is ready to be closed. Otherwise, a serious prejudice to the rights of other creditors would exist. In enacting Section 57d in 1938, Congress struck a balance between the interests of contingent creditors and proven creditors, with due and proper safeguard for the rights of *all creditors of the bankrupt.*

Therefore, at this juncture, the essential question is whether the disallowance of the Claimants' Claims under Section 57d of the Bankruptcy Act is improper. As urged under Point III, in order to evaluate this contention, the application of Section 57d must be considered in context of the present status of the bankruptcy proceeding and the posture of the two lawsuits commenced by the Claimants.

As noted hereinabove, the liquidation of the bankrupt's assets has been completed resulting in a present estate of approximately $800,000.00. The only administrative procedure that remains is the completion of the objections to claims. The Trustee expects that these objections will be resolved by the end of March, 1976, so that this estate should be ready to be closed immediately thereafter.

There are over 600 claims filed in this bankruptcy proceeding consisting of priority tax claims, administrative claims incurred during the Chapter XI proceeding and general claims. After payment of administrative expenses and the priority claims, it is anticipated that a dividend of between 18% and 20% will be available for the general unsecured creditors' claims which aggregate roughly $3,000,000.00.

As previously discussed herein, both actions commenced by the Claimants are in their initial stages. Class status has been denied in both law suits and in the first one (75 Civ. 731) the bankrupt's accounting firm has successfully moved for summary judgment which was affirmed by this Court of Appeals. Only appellant Eddie L. Thompson, Jr. remains as the plaintiff in both actions.

Not all the defendants in the law suits have been served and those that have appeared are vigorously defending them. The first action is almost two years old and the second one was commenced about one and one-half years ago. The allegations of both complaints involve many complex, difficult issues of fact and of law. It is expected that the discovery stage of both proceedings will take a very long period of time and that neither case will be ready for trial for quite some years. Taking into consideration the definite probability of various appeals, it is very possible that the *ultimate* determination of these law suits may take longer than the five to six years estimated herein, and may very well be as far off as eight or more years from today.

It must be remembered that the Claimants are at this point only *shareholders* of the bankrupt, not creditors thereof. The Claims are wholly disputed on the merits by the Trustee. Generally, shareholders do not participate in the distribution of the assets of a bankrupt corporation unless the creditors of the bankrupt are paid in full. It is clear from the amount of claims filed in this proceeding and from the available assets that there will only be a partial distribution to the general creditors. By suing the bankrupt corporation and seeking creditor status, the stockholder-Claimants are in effect maintaining an action against the creditors of this estate. It must be reiterated

that the Claims asserted by the Claimants are without merit and thoroughly contested by the Trustee.

Recognizing this situation, the Bankruptcy Judge stated:

> "The trial of the cases in the district court and ultimate disposition is so distant that I must find that liquidation of the claims would so unreasonably delay the administration of this estate that I must perforce exercise my discretion and pursuant to §§ 57d and 63d disallow and expunge the claims as not provable without prejudice to any determination of the pending class actions in the District Court". (21a).

Clearly, due regard *must be given* to the other creditors of this estate. Consider there are over 600 creditors with claims aggregating $3,000,000.00 and that this estate should be ready for closing within the next two months. The instant proceeding is indeed a classic case for the application of Section 57d of the Bankruptcy Act. On balance, the expeditious administration of bankrupt estates requires the proper application of Section 57d to certain situations. The case at bar falls within the perimeters of that allowable application.

It could very well be said that should the other 600 creditors of the bankrupt be made to wait from five to six years (if not longer) for their distributions, or should the Claimants' law suits be ultimately decided against them, then the other creditors of the bankrupt, in effect, have been denied due process by having to have waited an unreasonably long time for their just distribution in accordance with the provisions of the Bankruptcy Act. Manifestly, there was no abuse of discretion by the Bankruptcy Judge in his application of Section 57d to the Claims herein.

POINT V

Claims Nos. 533 and 534 are not properly class claims.

The Claimants have cited Rule 723 of the Rules of Bankruptcy Procedure on behalf of their assertion that class claims are proper in bankruptcy proceedings.

Rule 723, which incorporates Rule 23 of the Federal Rules of Civil Procedure, concerns only *adversary proceedings* as defined in Part VII of the Rules of Bankruptcy Procedure. Rule 23, F.R. Civ. P., makes provisions for and establishes the criteria for class actions in federal *litigation.*

Rule 23, F.R. Civ. P., has *not* been extended to any other bankruptcy procedure, including the filing of claims in a bankruptcy proceding. The assertion of a claim against a bankrupt estate is not an adversary proceeding and the Bankruptcy Rules regulating litigation are therefore not applicable. Without any further statutory authority, the application of Rule 23, F.R. Civ. P., to the filing of a proof of claim in the bankruptcy proceeding is unwarranted.

Stipulated facts No. 1 and No. 3 (13a) show that the Claims were filed by named individuals on ehalf of a purported class consisting of "diverse persons, firms, corporations, and associations." If the Claimants represented themselves as agents of the class, then they failed to comply with the Bankruptcy Rule 301(a) and Official Form No. 15, with reference to the required statements for a claim filed by an agent of a creditor.

The Claimants cite *In re Four Seasons Nursing Centers of America, Inc., supra,* (cited by Claimants at *CCH Bankr. Law Rptr.*, ¶ 64,976) in support of their contention that class claims are proper in *straight bankruptcy* proceedings. *Four Seasons* was a Chapter X in which the reorganization trustee recognized that one group of shareholders had a valid claim. The trustee therein compromised the claim of that particular group by providing in the plan of reorganization that the specific group of shareholders would be a separate class of creditors under the plan. *Four Seasons* dealt with differentiation of classes of creditors under a plan of reorganization and not with the filing of class claims in a straight bankruptcy proceeding. In Chapter X, the aim is the restructuring of a troubled company. Straight bankruptcy deals with liquidation and distribution of assets of a defunct entity. Thus, *Four Seasons* has no bearing to the case at bar.

Moreover, as previously noted herein, pursuant to an order made by Judge Frankel in both class action lawsuits commenced by the Claimants, neither lawsuit has been granted class action status.

Accordingly, the Claimants' reliance on Bankruptcy Rule 723 is misplaced and the Bankruptcy Judge was correct in disallowing Claims No. 533 and 534 insofar as they were filed on behalf of classes of persons other than those named as representatives in the respective claims.

CONCLUSION

The Bankruptcy Judge correctly found that Claims No. 533 and 534 filed in this bankruptcy proceeding were not class claims and that they were both unliquidated and contingent so as to fall within the proviso of Section 57d of the Bankruptcy Act. When the Bankruptcy Court's action is viewed in context of the present state of the bankruptcy proceeding and the status of the Claimants' lawsuits, the balance must be struck in favor of the applicability of Section 57d to the instant case.

The Bankruptcy Judge's decision and order were given appropriate countenance by the District Court which upheld the determinations made by the Bankruptcy Court.

In view of the foregoing, this appeal should be dismissed and the Order of Honorable Kevin T. Duffy dated November 3, 1975, which upheld the disallowance of Claims No. 533 and 534 by Judge Herzog, should be affirmed.

Respectfully submitted,

OTTERBOURG, STEINDLER HOUSTON & ROSEN, P.C.
Attorneys for Trustee-Appellee

Of Counsel:
CONRAD B. DUBERSTEIN, ESQ.
M. DAVID GRAUBARD, ESQ.

EXHIBIT "A"

Order of Judge Herzog Dated June 9, 1975

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

Index #73 B 679

In the Matter

—of—

CARTRIDGE TELEVISION, INC.,

Bankrupt.

ORDER DISALLOWING AND EXPUNGING
CLAIMS NO. 533 AND 534

The Trustee herein, having objected to Claim No. 533 and Claim No. 534 filed in this proceeding,

Now, upon the petition of STANLEY TULCHIN, Trustee herein, by his attorneys, dated January 2, 1975; the notice of motion thereon, dated January 3, 1975; the affidavit of service on file with this Court; the Answer of EDIE L. THOMPSON, JR., by his attorneys, dated January 14, 1975; the minutes of the hearing held before this Court on January 17, 1975; the stipulation of facts between the co-counsel for the Trustee and counsel for the claimants, dated March 24, 1975; the stipulation restoring motion to calendar between co-counsel for the Trustee and the attorneys for the claimants, dated April 9, 1975; the memoranda of law submitted in support of and in opposition to the motion; the hearing held and minutes taken before this Court on April 14, 1975; and after hearing OTTERBOURG, STEINDLER, HOUSTON &

Exhibit "A"

ROSEN, P.C., and WACHTELL MANHEIM & GROUF, ESQS., co-counsel for the Trustee, by M. DAVID GRAUBARD, ESQ., in support thereof, and BADER & BADER, ESQS., attorneys for claimant, by I. WALTON BADER, ESQ., in opposition thereto; and due deliberation having been had thereon; and the Court having rendered its decision, dated June 3, 1975, sustaining the Trustee's objections to Claim No. 533 and Claim No. 534; and it is further

FOUND, that Claim No. 533 and Claim No. 534, filed herein, are both unliquidated claims; and it is further

FOUND, that Claim No. 533 and Claim No. 534 are both not capable of liquidation or of reasonable estimation and that such liquidation or estimation would unduly delay the administration of this bankrupt estate; and

NOW, on motion of OTTERBOURG, STEINDLER, HOUSTON & ROSEN, P.C., and WACHTELL MANHEIM & GROUF, ESQS., co-counsel to the Trustee herein; it is

ORDERED, that Claim No. 533 be and the same hereby is deemed to be a claim filed individually by EDIE L. THOMPSON, JR. and ROBERT KELLER, and that Claim No. 534 be and the same hereby is deemed to be a claim filed by the nine persons specified therein; and it is further

ORDERED, that Claim No. 533, filed by EDIE L. THOMPSON, JR. and ROBERT KELLER and Claim No. 534, filed by nine specified claimants, both claims purportedly filed as class claims, be and the same hereby are disallowed insofar as the respective proofs of claim represent claims for unidentified persons other than those named in the two claims; and it is further

ORDERED, that Claim No. 533 and Claim No. 534, filed herein, are both disallowed and expunged as claims from this proceeding without prejudice to any determination of the pending class actions in the District Court.

Dated: New York, New York
June 9, 1975

/s/ ASA S. HERZOG
Bankruptcy Judge

EXHIBIT "B"

Order of Judge Duffy Dated November 3, 1975

ENDORSEMENT

73 B 679

The order appealed from is affirmed.
So ORDERED.

New York, New York
November 3, 1975

/s/ KEVIN THOMAS DUFFY
Kevin Thomas Duffy
U.S.D.J.

EXHIBIT "C"

Relevant Docket Entries of the Clerk, U.S.D.C., S.D.N.Y.

7/31/75 Filed NOTICE OF APPEAL to the District Court by E. Thompson Jr., R. Keller, E. Neff, S. Mancini, D. Ackerman, B. Copses, B. Diangiles, J. Magda, J. Johnson and D. Ellison, from an order of Hon. Asa S. Herzog, Bank. Judge Dated 7/9/75. Ret. September 16, 1975, at 10:30 A.M. in room 506.B.

7/31/75 Filed Designation of Record on Appeal. f.

9/ 9/75 Filed Trustee's Memorandum of Law in opposition to appeal from order disallowing and expunging claims No. 533 and 534. Sub By: Wachtel, Manheim & Grouf, Esqs.

9/10/75 Filed STIPULATION OF ADJOURNMENT, this matter on appeal is adjourned from 9/16/75 to 9/23/75. So ordered Werker, J. Dated 9/8/75. f.

11/12/75 Filed NOTICE OF APPEAL by Eddie L. Thompson, Jr., R. K. Keller, E. A. Neff, S. Mancini, D. D. Ackerman, B. Copses, B. Diangikes, J. F. Magda, J. Johnson and D. Ellison, to USCA from the order of Hon. K. Duffy, District Judge Affirming the order of Herzog, Bank., Jdg. m/n.

12/19/75 Filed Notice of Original Record transmitted to the USCA.

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

- -x

In the Matter : Docket No. 75-5019

-of- :

CARTRIDGE TELEVISION, INC., :

Bankrupt. :

- -x

EDDILE L. THOMPSON, JR., EDWARD A. NEFF, SUE MANCINI, DAVID D. ACKERMAN, BILL COPSES, BILL DIANGIKES, JOHN F. MAGDA, J. HIRAM JOHNSON, DEAN ELLISON, and ROBERT KELLER, as Pension Fund Trustee, :

AFFIDAVIT OF SERVICE TO APPELLEE'S BRIEF

Appellants,

-against-

STANLEY TULCHIN, as Trustee-in-Bankruptcy of Cartridge Television, Inc.,

Appellee.

- -x

FERN C. SKYLER, being duly sworn, deposes and says: deponent is not a party to the action, is over 18 years of age, and resides at New York, New York.

On February 17, 1976, deponent served the within three copies of the Appellee's Brief upon Bader & Bader, Esqs., attorneys for the Appellants herein, by personally leaving them with the attorneys at their offices, located at 270 Madison Avenue, New York, New York 10017. Deponent knew the person

so served to be the person mentioned and described in said papers as the attorneys for the Appellants herein.

Fern C. Skyler

FERN C. SKYLER

Sworn to before me this
17th day of February, 1976.

M. David Graubard

M. DAVID GRAUBARD
Notary Public, State of New York
No. 41-6629165
Qualified in Queens County
Commission Expires March 30, 1976

STATE OF NEW YORK, COUNTY OF ss.:

The undersigned, an attorney admitted to practice in the courts of New York State,

Check Applicable Box

☐ Certification By Attorney — certifies that the within has been compared by the undersigned with the original and found to be a true and complete copy.

☐ Attorney's Affirmation — shows: deponent is the attorney(s) of record f in the within action; deponent has read the foregoi and knows the contents thereof; the same true to deponent's own knowledge, except as to the matters therein stated to be alleged on information and beli and that as to those matters deponent believes it to be true. This verification is made by deponent and not by

The grounds of deponent's belief as to all matters not stated upon deponent's knowledge are as follows:

The undersigned affirms that the foregoing statements are true, under the penalties of perjury.

Dated:

.....
The name signed must be printed beneath

STATE OF NEW YORK, COUNTY OF ss.:

Check Applicable Box

☐ Individual Verification — being duly sworn, deposes and says: deponent the in the within action; deponent has re the foregoing and knows the contents thereof; the same is true deponent's own knowledge, except as to the matters therein stated to be alleged on information and belief, and to those matters deponent believes it to be true.

☐ Corporate Verification — the of a corporation, in the within action; deponent has read t foregoing and knows the contents thereof; and the sam is true to deponent's own knowledge, except as to the matters therein stated to be alleged upon information a belief, and as to those matters deponent believes it to be true. This verification is made by deponent becau is a corporation and deponent is an officer there

The grounds of deponent's belief as to all matters not stated upon deponent's knowledge are as follows:

Sworn to before me on 19

.....
The name signed must be printed beneath

STATE OF NEW YORK, COUNTY OF ss.:

being duly sworn, deposes and says: deponent is not a party to the actio is over 18 years of age and resides at

Check Applicable Box

☐ Affidavit of Service By Mail — On 19 deponent served the within upon attorney(s) for in this action, at the address designated by said attorney(s) for that purpo by depositing a true copy of same enclosed in a post-paid properly addressed wrapper, in — a post office — offici depository under the exclusive care and custody of the United States Postal Service within the State of New Yor

☐ Affidavit of Personal Service — On 19 at deponent served the within upon herein, by delivering a true copy thereof to h personally. Deponent knew th person so served to be the person mentioned and described in said papers as the

Sworn to before me on 19

.....
The name signed must be printed

NOTICE OF ENTRY

Sir:-Please take notice that the within is a *(certified)* true copy of a

duly entered in the office of the clerk of the within named court on 19

Dated,

Yours, etc.,

OTTERBOURG, STEINDLER, HOUSTON & ROSEN, P.C.

Attorneys for

Office and Post Office Address

230 Park Avenue

Borough of Manhattan New York, N. Y. 10017

To

Attorney(s) for

NOTICE OF SETTLEMENT

Sir:—Please take notice that an order

of which the within is a true copy will be presented for settlement to the Hon.

one of the judges of the within named Court, at

on the day of 19

at M.

Dated,

Yours, etc.,

OTTERBOURG, STEINDLER, HOUSTON & ROSEN, P.C.

Attorneys for

Office and Post Office Address

230 Park Avenue

Borough of Manhattan New York, N. Y. 10017

To

Attorney(s) for

Index No. 75-5019 Year 19

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In the Matter

-of-

CARTRIDGE TELEVISION, INC.,

Bankrupt.

AFFIDAVIT OF SERVICE

OTTERBOURG, STEINDLER, HOUSTON & ROSEN, P.C.

Attorneys for Bankrupt

Office and Post Office Address, Telephone

230 Park Avenue

Borough of Manhattan New York, N. Y. 10017

679-1200

To

Attorney(s) for

Service of a copy of the within

is hereby admitted.

Dated,

Attorney(s) for